UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF LOUISIANA

IN RE:

CAJUN ELECTRIC POWER COOPERATIVE, INC. **CIVIL ACTION NO. 94-2763-B2**

Debtor **BANKRUPTCY CASE NO. 94-11474**

REASONS FOR DECISION REGARDING
TRUSTEE'S OBJECTION TO CLAIMS OF MEMBERS
ARISING FROM REJECTION OF ALL-REQUIREMENTS CONTRACTS and
TRUSTEE'S MOTION FOR DETERMINATION UNDER RULE 3013 OF THE
PROPER CLASSIFICATION OF MEMBERS' REJECTION DAMAGE CLAIMS

Cajun Electric Power Cooperative, Inc. ("Cajun" or "Debtor") is a non-profit Louisiana electric cooperative corporation that generates and transmits wholesale electric power to its members (individually, "Member", collectively, "Members"). At the time of the filing of this chapter 11 proceeding on December 21, 1994 ("Petition Date"), Cajun consisted of the following 12 Louisiana cooperatives: Beauregard Electric Cooperative, Inc., Concordia Electric Cooperative, Inc. ("Concordia"), Dixie Electric Membership Corporation, Jefferson Davis Electric Cooperative, Inc., Northeast Louisiana Power Cooperative, Inc., Pointe Coupee Electric Membership Corporation ("Point Coupee"), South Louisiana Electric Cooperative Association, Southwest Louisiana

Electric Membership Corporation ("SLEMCO"), Valley Electric Membership Corporation, Washington-St. Tammany Electric Cooperative, Inc., Claiborne Electric Cooperative, Inc. ("Claiborne"), and Teche Electric Cooperative, Inc.[1] Each Member purchases electric power at wholesale from Cajun and in turn distributes that power at retail to its consumers, who are, generally, the rural citizens of the State of Louisiana.

The court has again concluded confirmation hearings regarding two separate plans of reorganization in this complex and sometimes controversial chapter 11 proceeding.[2] The plans presently under consideration by the court are the plan in which LaGen[3], the Official Committee of Unsecured Creditors, SLEMCO, Pointe Coupee, and Concordia are co-proponents ("Creditors' Plan"), and the plan in which SWEPCO[4] and the Committee of

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[1]Cajun and each Member was created pursuant to the provisions of the Louisiana Cooperative Law, LSA-R.S. 12:401, *et seq*.

[2]The court determined that neither of the prior plans were confirmable. In re Cajun Electric Power Cooperative, Inc.), 230 B.R. 715 (Bkrtcy. M.D. La. 1999).

[3]Louisiana Generating, L.L.C. LaGen is a Louisiana limited liability company, owned 40% by Southern Electric Company ("Southern"), and 30% each by NRG Energy, Inc. ("NRG") and Zeigler Coal Holding Company ("Zeigler").

[4]Southwestern Electric Power Company.

Certain Members ("CCM")[5] are co-proponents ("SWEPCO Plan").[6]

Two matters incidental to confirmation of the Creditor's Plan are presently before the court, namely, the **TRUSTEE'S OBJECTION TO CLAIMS OF MEMBERS ARISING FROM REJECTION OF ALL-REQUIREMENTS CONTRACTS** ("Trustee's Objection"), and **TRUSTEE'S MOTION FOR DETERMINATION UNDER RULE 3013 OF THE PROPER CLASSIFICATION OF MEMBERS' REJECTION DAMAGE CLAIMS** ("Trustee's Motion"). In these matters, respectively, the Trustee (1) objects to claims of the Members which may be asserted based upon the rejection of the All Requirement Contracts ("ARCs") in the Creditors' Plan and, (2) seeks a determination of the proper classification of any Member rejection claims under the Creditors' Plan, urging that such claims, if any, are subrogated by operation of law. These matters were heard along with confirmation on June 22-25, 1999.

The court has previously issued written opinions[7] discussing

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[5]An unofficial committee of seven members of Cajun Electric Power Cooperative, Inc.

[6]Subsequent to the conclusion of the confirmation hearings, the CCM withdrew its support of and SWEPCO withdrew the SWEPCO Plan.

[7]The Cajun Electric Members Committee v. Ralph R. Mabey (In re Cajun Electric Power Cooperative, Inc.), 230 B.R. 693 (Bkrtcy. M.D. La. 1999), and In re Cajun Electric Power Cooperative, Inc.), 230 B.R. 715 (Bkrtcy. M.D. La. 1999).

the ARCs, and will not repeat those discussions here. Suffice to say, however, that, pursuant to the ARCs, which were determined to be executory contracts, each Member is generally obligated to purchase from Cajun, and Cajun is obligated to sell to each Member, all of the Member's power requirements until the year 2021. The specific treatment of the ARCs under the Creditors' Plan is at the heart of the instant proceedings.

The Creditors' Plan provides for LaGen to purchase the Debtor's non-nuclear assets for a price in excess of $1 billion. The purchase price is then distributed pursuant to the Creditors' Plan to various classes of creditors, with no proposed distribution to equity holders, i.e., the Members. Members, however, in addition to their claims as holders of the Debtor's equity, are the holders of unsecured claims[8], which claims are not the subject of any dispute. The instant proceedings seek to address the situation which may occur under the Creditors' Plan if the ARCs are rejected pursuant to section

[8]In an earlier proceeding, the Trustee filed an objection to the proofs of claim filed by each Member. The parties entered into a stipulation that a portion of each claim was in fact properly filed as an unsecured claim. The dispute arose over the proper classification of the balance of such proofs which were based upon each Member's patronage capital credit account. The court determined that those claims were properly classified as equity rather than debt.

365 of the Bankruptcy Code[9].

The non-debtor party to a rejected executory contract is entitled to file a proof of claim for damages resulting from such rejection.[10] While the proponents of the Creditors' Plan contend the Members will have no claim resulting from rejection of the ARCs, the Creditors' Plan provides, with respect to any such potential claim, for the subordination thereof to the claims of other creditors.

The Creditors' Plan provides that each Member is offered its choice of five options with regard to their ARCs and future power supply. Specifically, each Member has the option to elect:

(1) to have its ARC rejected and thereafter obtain power in the future from any source it desires (including both LaGen and SWEPCO) and on such terms as it is able to negotiate;[11]

(2) to purchase power from LaGen for the short-term while the Member makes arrangements to obtain long-term power;

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[9]Title 11, United States Code. Further references herein to the Bankruptcy Code will be shown as "section ___."

[10]Rule 3002(c)(4), Federal Rules of Bankruptcy Procedure, provide that such claim may be filed within such time as the court may direct.

[11]The Creditors' Plan provides that this option is the "default option" in the event any Member fails to elect among the five options.

(3) to purchase power from LaGen under the long-term power contract proposed by LaGen ("LaGen PSSA") in connection with the Creditors' Plan;

(4) to purchase power from LaGen under the long-term power contract proposed by SWEPCO ("SWEPCO PSSA") in connection with the SWEPCO Plan; or

(5) to have its ARC assumed and assigned to any qualified entity the Member chooses pursuant to sections 365 and 1123.

LAW AND ANALYSIS

Two expert witnesses testified with respect to the potential amount of the Members' rejection damage claims: Judah Rose (live) on behalf of SWEPCO, and Dr. Michael Yokell (by deposition) on behalf of the Trustee. At the conclusion of the hearing on June 25, 1999, and prior to reviewing Dr. Yokell's deposition testimony, the court annunciated what it believed to be the appropriate analysis for determining the Members' rejection damage claim, if any.[12] Having now reviewed post-hearing argument submitted by the parties, and having once again reexamined the law on this issue, the court maintains its belief that the announced analysis is appropriate.

Section 365(g) provides in relevant part that:

(g) . . . the rejection of an executory contract

[12]See Transcript 6/25/99 at 172:13 - 176:8.

> . . . of the debtor constitutes a breach of such contract . . . -
>
> > (1) if such contract . . . lessee has not been assumed under this section or under a plan confirmed under chapter 9, 11, 12, or 13 of this title, immediately before the date of the filing of the petition; . . .

Thus, the rejection of an executory contract constitutes a breach of that contract with the breach being deemed to have occurred prepetition. See Stewart Title Guaranty Co. v. Old Republic National Title Ins. Co., 83 F.3d 735, 741 (5th Cir. 1996). With respect to a determination of damages flowing to the nondebtor party from such breach, bankruptcy courts must look to remedies specified by relevant state law. Ibid.

Louisiana law provides that "An obligor is liable for the damages caused by his failure to perform a conventional obligation. . . . La. Civ. Code. art. 1994[13]. The measure of damages is the "loss sustained by the obligee and the profit of which he has been deprived." Art. 1995. Where the obligor was not in bad faith, the only damages recoverable were those that were "foreseeable at the time the contract was made." Art. 1996.

Therefore, placing bankruptcy and Louisiana law in proper context, and in order to determine rejection damages, the court

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[13] Further references herein to the Louisiana Civil Code will be shown as "art. ___."

must first determine, as of the day before the Petition Date, and based upon facts in existence at that time, each Member's cost to obtain electricity under the ARCs over the remaining life of the contract, present valued as of the date of the breach. This number would then be compared to the present value of the cost which the Member would pay for electricity in the open market for the same period of time, using the same starting date and assuming the same set of facts. The difference between the two numbers, assuming that the latter (open market) is higher than the former (ARCs), is the starting point in the calculation of damages under Louisiana law. If, on the other hand, the open market cost is found to be less than the cost of power under the ARCs, no damages would arise from the rejection of the ARCs.

Mr. Rose concluded that the total damages which would result from the rejection of the Member ARCs would be in excess of one billion dollars. In order to arrive at this conclusion, Mr. Rose employed what has been referred to as a "but-for-breach" analysis in the calculation of damages. Under this analysis, Mr. Rose's assumptions in calculating both the cost of purchasing power on the market and the cost under the ARCs included the fact that Cajun had filed for bankruptcy, as well as factors which specifically resulted from the filing and

circumstances which have actually occurred since the filing.

Dr. Yokell, on the other hand, employed what has been referred to as a "but-for-bankruptcy" analysis, pursuant to which he calculated the cost to buy power under the ARCs using the day before the Petition Date as the starting point. Under this analysis, Dr. Yokell used facts in existence at that time, including the existing fuel contracts, the debt to the RUS[14] and continued regulation by the Louisiana Public Service Commission ("LPSC") utilizing traditional rate-making principles. The following were the only assumptions employed by Dr. Yokell: (1) the interest paid on the assets would be 8.99%, the interest rate approved by the LPSC in the 1990 Debt Restructure Agreement; (2) the proceeds from the contract under which Cajun sells power to SWEPCO would continue to be paid directly to the RUS; and (3) Cajun would continue to have a times interest earned ratio ("TIER") of 1.05, the TIER approved by the LPSC, prior to the bankruptcy, in its 1994 Rate Order. With these assumptions in hand, Dr. Yokell then calculated the amount which the Members would have to pay for electricity if they had gone to the market to obtain electricity for the remaining term of

[14]The United States, through the Rural Utilities Service, which is the successor to the Rural Electrification Administration. RUS is Cajun's largest creditor, and is currently owed in excess of $4 billion.

the ARCs.

Dr. Yokell testified that he calculated the difference between the market rate and the but-for-bankruptcy rate in net present value terms to be $230 million. However, since SLEMCO, Pointe Coupee, and Concordia have waived any claim for rejection damages under the Creditors' Plan and since Teche's ARC is to be terminated by mutual agreement without damages,[15] the difference is thus reduced to $161 million. Finally, Dr. Yokell calculated the costs to the Members under both the LaGen PSSA and the SWEPCO PSSA, and concluded that the costs to the Members under either of these options were lower than the but-for-bankruptcy cost.

Dr. Yokell's analysis satisfies the standards for determining damages under applicable law. Accordingly, the court accepts the calculations performed by Dr. Yokell, as they have been performed using the appropriate criteria. Conversely, the court rejects Mr. Rose's analysis as he did not employ the standards required by bankruptcy and Louisiana law. In

[15]Pursuant to the Interim Wholesale Power Contract between Teche, CLECO, and Cajun and as part of CLECO's acquisition of Teche, the parties agreed that CLECO would perform Teche's obligations under its ARC until the Effective Date of a confirmed plan of reorganization, at which time Teche's ARC would be voluntarily terminated by mutual agreement and would be replaced with a long-term contract between the purchaser of Cajun's assets under the plan and CLECO.

calculating damages, Mr. Rose took into account certain facts which have occurred since and as a result of the bankruptcy. Mr. Rose employed this technique as being more "realistic." Although the "but-for-breach" analysis may take into account more present facts, the Bankruptcy Code requires that the court essentially take a snapshot of the situation as it existed on the day before the filing of the bankruptcy petition. The basic fault, therefore, of Mr. Rose's analysis is that in calculating the Members' cost under the ARCs, he employed what the Members' rates would be emerging from bankruptcy, taking into account those benefits bestowed in bankruptcy. Further, Mr. Rose's analysis also runs afoul of Louisiana law which limits damages to those that were foreseeable at the time the contract was made. Art. 1996. The court can find no legitimate basis for assuming that the benefits to Members that Mr. Rose takes into account, i.e., those which exist due to the filing of the bankruptcy, were foreseeable at the time these contracts were entered into in the late 1970's. For these reasons, the court finds that Mr. Rose's analysis is faulty in that it did not employ the standards required by bankruptcy and Louisiana law. Dr. Yokell's analysis did apply the appropriate standard and his calculations will be accepted by the court for purposes of calculating possible rejection damages to the Members.

Accordingly, the court concludes that the difference between the amount which the Members would pay under the ARCs and the amount which they would pay to obtain power on the market is $161 million.

As previously indicated, however, this number is but the starting point in the calculation of damages under Louisiana law. We say starting point because under Louisiana law, a party must make "reasonable efforts to mitigate the damage caused by the obligor's failure to perform." Art. 2002. In discussing mitigation of damages, the court said in Boehm v. French, 548 So.2d 12, 13-14 (La. App. 5th Cir. 1989):

> Louisiana law requires an injured party to mitigate his/her damages. Unverzagt v. Young Builders, Inc., 252 La. 1091, 215 So.2d 823 (1968); Easterling v. Halter Marine, Inc., 470 So.2d 221 (La.App. 4 Cir. 1985), writ denied, 472 So.2d 920 (La.1985); Gagnet v. Zummo, 487 So.2d 721 (La.App. 5 Cir.1986). The duty to mitigate requires the injured party to take reasonable steps to minimize the damages that are a consequence of the injury. Unverzagt v. Young Builders, Inc., supra, Easterling v. Halter Marine, Inc., supra. These efforts are determined by the rules of "common sense, good faith and fair dealing." Unverzagt 215 So.2d at 825.

To determine if the Members have made "reasonable efforts to mitigate the damage" caused by the rejection, the court must next look to the options available to the Members in determining mitigation. In making such review, and assuming other factors are equal, the court assumes that the Members, as fiduciaries,

would select the option available to them which would result in the lowest amount of damages.

As observed hereinabove, the Creditors' Plan provides each Member with five options concerning the Member's ARC and the Member's future power supply. The court concludes that, under at least three of the options, the Members will suffer no damages whatsoever. First, a Member can elect to have their ARC assumed and assigned to an entity of their choice. The issue of rejection damages would not even arise under this option as the same contract would continue in existence. Second, the Members can elect to obtain power from LaGen under either the LaGen PSSA or SWEPCO PSSA. Under either scenario, according to Dr. Yokell's analysis, the Members would not suffer damages, but would enjoy a substantial benefit, as the cost of power over the life of either contract would be less than the cost of power under both the open market and ARCs analyses.

The Members argue that the duty to mitigate cannot require them to enter into a contract with the breaching party. This argument is rejected for two reasons. First, LaGen is not the breaching party, Cajun is. LaGen is not even a party to the ARCs. Second, under the Creditors' Plan, the Members make the decision of whether or not to have their contracts rejected. As noted above, the Members can choose to have their ARCs assumed

and assigned to an entity of their choice.

SWEPCO and LaGen have been vying for the opportunity to acquire Cajun's non-nuclear assets from the day the initial plans were filed in this case in 1995. From that day forward, the CCM, or its predecessor, has been supportive of SWEPCO's efforts. The practical consequence of this position is that the CCM has zealously, vociferously, and continuously opposed LaGen's endeavors to acquire these assets. No legal genius is required to see that the Members who are participants of the CCM desire to deal with SWEPCO rather than LaGen.

Nonetheless, the court is perplexed that the battle continues to rage in view of the options available to the Members under the Creditors' Plan. The CCM apparently negotiated an acceptable long-term power supply contract with SWEPCO, the SWEPCO PSSA. If the Members are not happy with the rate proposed by the LaGen PSSA, they have the option of selecting the SWEPCO PSSA. Thus, regardless of which plan is confirmed, the Members who previously supported the SWEPCO Plan will have the same rate for their long-term power supply, a rate they are ostensibly satisfied with as they voted to support the SWEPCO Plan and accept the SWEPCO PSSA.

Claiborne also argues that, in addition to the costs of obtaining power, the Members will sustain additional damages as

a result of the rejection of the ARCs. Claiborne contends if the ARCs are rejected, each Member may, at various times in the future, be required to pay the costs of constructing additional transmission facilities. Under the ARC's Cajun presently pays for these costs. If the ARCs are rejected, each Member will be on its own with regard to constructing transmission facilities that may become necessary in the future.

This position is without merit for several reasons. First, under the ARCs, although Cajun pays the transmission costs, such costs are passed through to the Members through Cajun's rate base. Thus, even though Cajun may initially pay these costs, ultimately each Member pays its proportionate share. Second, the Members have the option of having their ARCs assumed and assigned to another entity, which option will result in no damages. Finally, under the SWEPCO Plan, the Members would have been required to pay these costs. Yet, in their support of the SWEPCO Plan, the Members elected to waive any such damages. While this final factor may not be determinative of the issue, the court finds that the fact that the Members agreed to waive any such possible damages under the SWEPCO Plan was an indication that the Members themselves do not seriously believe that these possible costs are significant.

CONCLUSION

Based upon the foregoing reasons, the court finds that, under the Creditors' Plan, no Member rejection damages exist. Accordingly, the Trustee's Objection is **SUSTAINED**, and the Trustee's Motion is **DENIED as MOOT**.

A separate order in conformity with the foregoing reasons have this day been entered into the record of this proceeding.

THUS DONE AND SIGNED in Chambers, at Opelousas, Louisiana, this 31st day of August, 1999.

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Gerald H. Schiff
United States Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF LOUISIANA

IN RE:

CAJUN ELECTRIC POWER COOPERATIVE, INC. **CIVIL ACTION NO. 94-2763-B2**

Debtor **BANKRUPTCY CASE NO. 94-11474**

ORDER ON TRUSTEE'S OBJECTION TO CLAIMS OF MEMBERS ARISING FROM REJECTION OF ALL-REQUIREMENTS CONTRACTS and TRUSTEE'S MOTION FOR DETERMINATION UNDER RULE 3013 OF THE PROPER CLASSIFICATION OF MEMBERS' REJECTION DAMAGE CLAIMS

Presently before the court are the TRUSTEE'S OBJECTION TO CLAIMS OF MEMBERS ARISING FROM REJECTION OF ALL-REQUIREMENTS CONTRACTS ("Trustee's Objection"), and TRUSTEE'S MOTION FOR DETERMINATION UNDER RULE 3013 OF THE PROPER CLASSIFICATION OF MEMBERS' REJECTION DAMAGE CLAIMS ("Trustee's Motion"). These matters were heard along with confirmation on June 22-25, 1999. Following those hearings, the court took the matters under advisement. Now, for the written reasons this day filed into the record of this proceeding,

IT IS ORDERED that the Trustee's Objection is **SUSTAINED** ; and

IT IS FURTHER ORDERED that the Trustee's Motion is **DENIED as MOOT.**

THUS DONE AND SIGNED in Chambers, at Opelousas, Louisiana, this 31st day of August, 1999.

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Gerald H. Schiff
United States Bankruptcy Judge